Capital Budgeting Tools

Class Exercise

1. You've been hired to consult for a local parks and recreation department for Pawnee, Indiana. The new city manager, Ron Swanson, has decided that all new projects must be a net positive for the city, i.e., they must have a positive NPV. Ben, the city accountant has set the required return at 5%. The city is also concerned with how long it takes to recoup the initial investment and has set a 2.5 year payback period limit. Leslie and her team have proposed three projects for you to evaluate: i) Petting Zoo ii) Aquatics Center iii) Outdoor Concert Series. The cash flows from those projects are listed below.

Year	Petting Zoo	Aquatics Center	Outdoor Concert Series
0	-150,000	-2,500,000	-25,000
1	30,000	380,000	21,000
2	35,000	425,000	28,000
3	40,000	520,000	-20,000
4	45,000	735,000	65,000
5	45,000	950,000	-75,000

   (a) Calculate the metrics to make a proper decision on each project?

   (b) Make the accept reject decision for each project (assume independence).

   (c) What is a potential issue with "Outdoor Concert Series" cash flows? When should you accept this project?

   (d) Due to the availability of land the Parks Department can only pursue either the Petting Zoo project or the Aquatics Center. Which project should you accept?